Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matters of	)	
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Verizon's Petition for Waiver of Pricing	)	
Flexibility Rules for Fast Packet Services	)	WC Docket No. 04-246
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AT&T *OPPOSITION* TO VERIZON'S PETITIONS FOR WAIVER OR, ALTERNATIVELY, FORBEARANCE TO ALLOW IT TO EXERCISE PRICING FLEXIBILITY FOR FAST PACKET SERVICES

Leonard J. Cali
Lawrence J. Lafaro
Judy Sello
AT&T Corp.
Room 3A229
One AT&T Way
Bedminster, NJ 07921
(908) 532-1846

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Pursuant to the Wireline Competition Bureau's Public Notice,[1] AT&T Corp. ("AT&T") submits this *opposition* to Verizon's petition for waiver of Section 69.729 of the Commission's pricing flexibility rules and paragraph 173 of the Commission's *Pricing Flexibility Order*[2] to permit it to exercise pricing flexibility for certain advanced services that rely on packetized technology, including Frame Relay, Asynchronous Transfer Mode ("ATM"), and other packet-switched services other than DSL ("Advanced Services"), in those areas where Verizon has already obtained pricing flexibility for

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[1] *Pleading Cycle Established for Comments on Verizon's Petition for Waiver, or, Alternatively, Forbearance, to Allow it to Exercise Pricing Flexibility for Fast Packet Services,* WC Docket No. 04-246, DA 04-2116 (July 13, 2004).

[2] *See Access Charge Reform*, CC Docket No. 92-262, Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd. 14221 (1999) ("*Pricing Flexibility Order*"), *aff'd, WorldCom, Inc. v. FCC*, 238 F.3d 449 (2001).

traditional special access services.[3] Alternatively, in a separate petition, Verizon requests that, in the absence of a waiver, the Commission exercise its authority pursuant to section 10 of the Communications Act of 1934, as amended,[4] to forbear from enforcing section 69.729 of the Commission's rules and paragraph 173.[5] The Commission should *deny* these petitions. Verizon cannot obtain pricing flexibility through the particular waivers and forbearance it seeks; neither waiver nor forbearance could remotely be justified in these circumstances or on the bases Verizon asserts; and relief would particularly be inappropriate as the Commission considers closely related issues in an ongoing, comprehensive proceeding.

INTRODUCTION AND SUMMARY

As Verizon explains,[6] pursuant to the terms of the *Bell Atlantic / GTE Merger Order,* it transferred its advanced services from the Verizon telephone companies into a separate affiliate, known as Verizon Advanced Data Inc. ("VADI"), so as to provide these services on an unregulated basis. Subsequently, in *ASCENT v. FCC*, 235 F.2d 662 (D.C. Cir. 2001), the Court overturned the rationale of the merger order with the result

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[3] Petition for Waiver of Pricing Flexibility Rules for Fast Packet Services, WC Docket No. 04-246, Verizon Petition for Waiver to Allow it to Exercise Pricing Flexibility for Advanced Services where the Commission has Granted Relief for Traditional Special Access Services (filed June 25, 2004) ("*Verizon Waiver Petition*").

[4] *See* 47 U.S.C. § 160 *et seq.*

[5] Petition for Forbearance under 47 U.S.C. Section 160(c) from Pricing Flexibility Rules for Fast Packet Services, WC Docket No. 04-246, Verizon Petition, in the Alternative, for Forbearance to Allow it to Exercise Pricing Flexibility for Advanced Services where the Commission has Granted Relief for Traditional Special Access Services (filed June 25, 2004) ("*Verizon Forbearance Petition*").

[6] Memorandum of Points and Authorities in Support of Verizon's Petition for Waiver of Pricing Flexibility Rules and Contingent Petition for Forbearance, attached to Verizon's Waiver and Forbearance Petitions, filed June 25, 2004 ("*Verizon Mem.*"), at 2-4.

that VADI would be treated as a successor or assign of the Verizon operating companies, which - under the terms of the merger order - triggered a termination of the separate affiliate requirement for Verizon's advanced services. Consequently, at Verizon's initiative, these services were transferred to the Verizon operating companies that now offer them under Verizon Tariff F.C.C. No. 20. Although Verizon offers its advanced services under its interstate tariffs, the Wireline Competition Bureau granted, at Verizon's request, waivers of Section 61.42(g) of the Commission's rules so that Verizon would *not* be required to incorporate these advanced services in price caps in the 2002, 2003 and 2004 annual access filings.[7] As a result of these interim waivers, Verizon states that these advanced services were not incorporated into its annual access tariff filings according to paragraph 173 of the *Pricing Flexibility Order* ("Whenever a price cap LEC can demonstrate in an annual access tariff filing that one of its new services would be properly incorporated in a basket or service band for which there has been granted Phase I or Phase II regulatory relief in any MSA or MSAs, it will be granted the same relief in the same MSAs for that new service.").

Verizon indicates that the advanced services at issue consist of services that rely on advanced packet-switched technology or "Fast Packet Services," such as Frame Relay, ATM, and other advanced packet-switched technologies (other than DSL) and the special access circuits used to deliver them, in geographic areas for which the Commission has already granted Phase I or Phase II pricing flexibility for special access services

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[7] *Verizon Petition for Waiver of the Commission's Price Cap Rules,* 19 FCC Rcd. 7095 (2004); *Verizon Petition for Interim Waiver of Section 61.42(g) of the Commission's Rules,* 18 FCC Rcd. 6498 (2003); *Verizon Petition for Interim Waiver of Section 61.42(g), 61.38, and 61.49 of the Commission's Rules,* 17 FCC Rcd. 11,010 (2002) (collectively the "*Verizon Interim Waiver Orders*").

generally. *Verizon Mem.* at 5. Verizon contends that because it has already made the competitive showing necessary to obtain pricing flexibility for its traditional special access services, there is no point to either requiring these advanced services to be incorporated into price caps *or* to require additional market-by-market competitive showings in order to obtain the same relief that Verizon has already been granted for traditional special access services. *Verizon Mem.* at 7-8.

Contrary to Verizon's assertions, Verizon has not and cannot show that it is entitled to pricing flexibility for its advanced packet-switched services via either waiver *or* forbearance. As shown in Section I, the Commission has already indicated that it never intended these advanced or "non-traditional" access services to be governed by the deregulatory processes established by the *Pricing Flexibility Order*, and is instead considering such broad relief as part of the *Dom/Nondom* proceeding. In addition, Verizon cannot obtain pricing flexibility through waiver or forbearance because advanced packet-switched services were never part of the price cap regime to which pricing flexibility applies, and their regulatory status is currently under review in the *Dom / Nondom* proceeding. For both these reasons, Verizon's waiver and forbearance petitions, even if granted, would not and cannot yield the pricing flexibility relief that Verizon seeks.

In all events, as discussed in Section II, Verizon has not justified a waiver or forbearance because it has not shown "special circumstances" warranting a waiver nor presented the detailed market analyses that are required in any forbearance petition demonstrating that competition and consumers would not be harmed if forbearance were granted. Verizon never identifies the source of the restrictions on its pricing flexibility

(as opposed to the restrictions on the Commission's provisions for deregulating "traditional special access services") and thus never justifies why such provisions should be subject to waiver or forbearance. Nor does Verizon point to any overbroad rule or requirement that requires relief in the particular circumstances; indeed, it admits that the "individualized" relief it has already sought and secured is what now prompts these additional petitions for relief. Nor does it indicate why it should not have to provide such services through a separate affiliate, as the Commission has elsewhere required as a condition of permitting pricing flexibility for advanced services. And even if Verizon were entitled to relief from the Commission's provisions for *deregulation*, it has not begun to justify such relief. It has not, for example, shown that particular markets for the services it identifies are currently competitive and does not address the principal risks to competition (especially through the increased threat of discrimination and, in particular, price squeezes) that the Commission has identified and that are most directly raised by the petitions. Prominently, Verizon's market assertions fail to distinguish between local *and* interLATA advanced services and totally distort the status of competition in local markets. Because of Verizon's dominance in the local advanced services market, any grant of pricing flexibility would permit it to engage in anticompetitive price squeezes and discriminatory pricing.

Moreover, as shown in Section III, the Commission should *not* expand pricing flexibility to advanced services at this time, given that the Bells' market behavior following grants of pricing flexibility for traditional special access services confirms the noncompetitive nature of special access markets, and AT&T and others have sought *Mandamus* relief requiring the Commission to revamp that failed regime. If

notwithstanding these marketplace realities, and the pendency of *Mandamus* and the *Dom / Nondom NPRM,* the Commission were inclined to even consider pricing flexibility for advanced services (which it should *not*), the Commission should be developing a more stringent pricing flexibility test and require Verizon to comply with that. Given the change in market conditions, with numerous competitors exiting local markets since Verizon's pricing flexibility grants, at a minimum, Verizon must be required to show, using a detailed analysis of local market conditions, that such pricing flexibility is justified. For these reasons, the Commission should *deny* the relief sought in Verizon's waiver and forbearance petitions.

ARGUMENT

I. VERIZON CANNOT OBTAIN PRICING FLEXIBILITY FOR ADVANCED SERVICES THROUGH THE WAIVER OR FORBEARANCE IT SEEKS.

Verizon contends that but for the fact that it has been permitted to exclude its advanced services from price caps because of the price cap waivers it has obtained, it would have been entitled to a grant of pricing flexibility when it obtained such relief on an MSA-by-MSA basis for traditional special access services. *Verizon Mem.* at 6. Because the waivers preclude Verizon from including its advanced services in price caps, it contends that it may get pricing flexibility through either waiver of, or forbearance from, the pricing flexibility rules. Verizon is wrong.

The Commission has recognized that incumbent LECs' advanced services are distinct from the "traditional special access" services that are covered by the *Pricing Flexibility Order* and the deregulatory pricing flexibility structure that the order established – and which Verizon now seeks to have apply to its advanced services. *See*

Review of Regulatory Requirements for Incumbent LEC Broadband Telecommunications Services, 16 FCC Rcd. 22745, ¶ 22 (2001) ("*Dom / Nondom NPRM*") (defining services subject to the *Dom / Nondom* proceeding as including Frame Relay and ATM services, and "not[ing] that we are not considering whether traditional special access services belong in the larger-business market for advanced services as these services are governed by the Commission's pricing flexibility regime."). Verizon's own petitions expressly acknowledge (in their very headings) that the services subject to the petitions are not such "traditional special access services."[8] And maintaining the distinction between such traditional special access services subject to the *Pricing Flexibility Order*'s deregulatory processes and the advanced services subject to the *Dom / Nondom* proceeding makes sense of both proceedings. The *Pricing Flexibility Order* established its deregulatory processes based on its consideration of the traditional special access services that are crucial inputs required by the advanced services at issue in Verizon's petition – and to provide the advanced retail services of AT&T and others that compete against Verizon. The order's deregulatory processes were also crafted based on consideration of the particular competitive issues underlying these traditional special access services, not the very different competitive conditions surrounding the retail advanced ATM, Frame Relay and Virtual Private Network ("VPN") services that Verizon would now have the Commission address. And, indeed, the Commission is addressing these very services and these very different competition issues in its *Dom / Nondom* proceeding. Granting Verizon's petitions, which would provide it with the principal relief Verizon seeks in the *Dom / Nondom* proceeding, would entirely subvert that broader rulemaking proceeding.

[8] *See Verizon Waiver Petition* at 1; *Verizon Forbearance Petition* at 1.

The Commission's observation that advanced services are *different* from those traditional special access services that can be subject to pricing flexibility is consistent with the Commission's prior regulatory treatment of packet-switched services and points to an additional, more fundamental reason why granting Verizon's petitions would not lead to the pricing flexibility that Verizon seeks. In its initial *1990 Price Cap Order*, the Commission concluded that price cap LECs must *exclude* certain services, such as packet-switched services, from price cap regulation.[9] The rationale for this longstanding requirement – "some offerings that currently appear in the LECs' federal tariffs do not lend themselves to incentive-based regulation, or raise significant and controversial issues that should be resolved outside of the price cap arena"[10] – is acutely applicable today, especially as applied to loop-based packet-switched incumbent services. Thus, Verizon assumes *incorrectly* that these advanced packet-switched services were intended to be *within* price caps, which is the threshold showing for pricing flexibility. *See* 47 C.F.R. § 69.701. Moreover, Verizon does not – and cannot – deny that advanced packet-switched loop-based services offered today engender "significant and controversial" regulatory classification, cost allocation, and other fundamental Title II issues that the Commission has not yet addressed, and which are now being considered in the *Dom / Nondom* proceeding,[11] as well as the *Wireline Broadband* proceeding.[12]

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[9] *Policy and Rules Concerning Rates for Dominant Carriers,* Second Report and Order, 5 FCC Rcd. 6786 (1990) ("*1990 Price Cap Order*").

[10] *1990 Price Cap Order,* ¶¶ 191, 195.

[11] Nor do the Bureau's decisions to grant Verizon a limited interim waiver in 2002-2004 to exclude from price caps the advanced services it reintegrated from its affiliate, VADI, into its operating companies somehow support Verizon's request in this proceeding. In the *Verizon Interim Waiver Orders*, the Bureau ruled only that the unique and special circumstances associated with reintegrating advanced services back into the parent company merited a limited interim waiver for those services to "allow maintenance of the

II. VERIZON HAS NOT JUSTIFIED A WAIVER OR FORBEARANCE TO ATTAIN PRICING FLEXIBILITY FOR ITS ADVANCED SERVICES.

The most glaring inadequacy in Verizon's petitions is that they never point to the source of the constraint on Verizon's pricing flexibility for advanced services – as opposed to the limitation on deregulation set forth in 47 C.F.R. § 69.729 – or seek to justify why Verizon should be relieved from that unmentioned constraint through a waiver or forbearance. For this reason alone, it would be arbitrary and capricious to grant the petitions.

In addition, Verizon can point to no special circumstances that justify waiver of or forbearance from an otherwise overbroad rule. A waiver is intended to ameliorate the effect of an overbroad rule that is not in the public interest as applied to a given situation.[13] Forbearance is similarly available where application of a rule is inappropriate in particular circumstances.[14] Verizon has already gotten individualized consideration in its price cap waivers. Indeed, Verizon admits that the results of the relief it has sought in

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status quo" until the Commission fully considered the issues related to the *Dom / Nondom NPRM* proceeding. *2003 Verizon Interim Waiver Orders* at ¶ 8 (emphasis added). The *Verizon Interim Waiver Orders* do not help Verizon in its effort to *change – rather than maintain – the status quo* for its packet-based services. In addition, Verizon's reliance on the *BellSouth Pricing Flexibility Order* is also misplaced. *See Verizon Mem.* at 6 and n.14, citing *BellSouth Petition for Pricing Flexibility for Special Access and Dedicated Transport Services*, 16 FCC Rcd. 18174 (2001). Indeed, the most that can be said about this order is that no party challenged BellSouth's decision to include ATM and Frame Relay services within its trunking basket price cap index when introduced in the mid-1990s.

[12] *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, Notice of Proposed Rulemaking, 17 FCC Rcd. 2019 (2002) ("*Wireline Broadband NPRM*").

[13] *See generally, e.g., WAIT Radio v. FCC*, 418 F.2d 1153, 1157 (D.C. Cir. 1969).

[14] *See* 47 U.S.C. § 160(a).

the past are the source of the constraint that it now petitions to have removed. Basic principles of equitable estoppel should preclude the relief Verizon now seeks.

Although Verizon expressly seeks a waiver / forbearance only from certain pricing flexibility rules, Verizon is actually seeking relief from: (i) the price cap waivers it obtained, (ii) the *1990 Price Cap Order* that excluded packet-switched services from price caps, *and* (iii) whatever substantive regulatory restraints preclude Verizon from offering packet-based services through individual contracts – relief that was *not* intended for advanced services offering by an incumbent LEC other than through a separate subsidiary. This, of course, is a broad attack on the general rules and does not remotely justify the "special circumstances" that Verizon must show to obtain a waiver. In all events, until the issues as to the appropriate regulatory treatment of incumbent LEC advanced services are resolved in the *Dom / Nondom NPRM* and *Wireline Broadband NPRM*, it would not be in the public interest to permit Verizon to obtain a waiver or forbearance to gain pricing flexibility for advanced services.

In addition, the Commission has already determined that pricing flexibility for such services is appropriate where, but only where, the RBOC provides those services through a separate affiliate,[15] but Verizon has not even shown why this reasoning should not apply to require denial of its petitions or why it cannot seek to take advantage of this precedent rather than securing extraordinary relief from the Commission in the form of a waiver or forbearance. A *separate subsidiary* is the mechanism for pricing flexibility for

[15] *See Review of Regulatory Requirements for Incumbent LEC Broadband Telecommunications Services*, 17 FCC Rcd. 27000 (2002) (forbearance from tariff regulation of SBC's advanced services granted only to the extent those services are provided through a structurally separate affiliate and subject to other commitments designed to protect consumers from risks to competition).

advanced services, and Verizon could have kept its advanced services in a separate subsidiary. To the extent its merger conditions required a waiver for it to pursue that course, it could have applied for such a waiver to keep these services in a separate subsidiary distinct from its operating company.

Even if a waiver or forbearance were an appropriate path to obtain pricing flexibility for advanced services, which for the reasons discussed above it is *not*, Verizon has failed to make the necessary showings. An "applicant [for waiver] faces a high hurdle even at the starting gate." *Telecommunications Relay Services Order*, 2004 WL 1469354, ¶ 110 (June 30, 2004). The movant must demonstrate that a waiver is "in the public interest" and the Commission may "only waive a provision of its rules for 'good cause shown.'" *Id.* In making these determinations, "[t]he Commission must take a 'hard look' at applications for waiver and must consider all relevant factors when determining if good cause exists" and it "must explain why deviation better serves the public interest, and articulate the nature of the special circumstances, to prevent discriminatory application and to put future parties on notice as to its operation." *Id.*; *see also Industrial Broadcasting v. FCC*, 437 F.2d 680, 683 (D.C. Cir. 1970) (applicant bears heavy burden to demonstrate that its arguments for waiver are substantially different from those which have been carefully considered at rulemaking proceeding). Verizon falls well short of its "heavy burden of showing good cause." *Telecommunications Relay Service Order,* ¶ 110.

Similarly, Verizon does not remotely satisfy the statutory criteria for forbearance under § 10(a) of the Communications Act, 47 U.S.C. § 160. The proponent of forbearance must make three "conjunctive" showings, and the Commission must "deny a

petition for forbearance if it finds that any one of the three prongs is unsatisfied." *CTIA* v. *FCC*, 330 F.3d 502, 509 (D.C. Cir. 2003). First, the proponent of forbearance must show that enforcement of the specific regulations at issue to the specific services at issue "is not necessary to ensure that the charges . . . are just and reasonable and not unjustly or unreasonably discriminatory." 47 U.S.C. § 160(a)(1). Second, it must show that enforcement of those regulations "is not necessary for the protection of consumers." *Id.* § 160(a)(2). And, third, it must show that non-enforcement of those regulations "is consistent with the public interest," *id.* § 160(a)(3), and, in particular, that such non-enforcement will "promote competitive market conditions" and "enhance competition among providers of telecommunications services," *id.* § 160(b).

Because the forbearance criteria focus on competition and consumer protection, both courts and the Commission have recognized that the Commission must examine *detailed evidence* concerning the markets for the specific services at issue. In particular, a request that seeks "the forbearance of dominant carrier regulation under Section 10" demands "a painstaking analysis of market conditions" supported by empirical evidence. *WorldCom, Inc. v. FCC*, 238 F.3d 449, 459 (D.C. Cir. 2001); *AT&T Corp.* v. *FCC*, 236 F.3d 729, 735-37 (D.C. Cir. 2001). The Commission has recognized that it cannot simply "assume that, absent" the regulation at issue, "market conditions or any other factor will adequately ensure that charges . . . are just and reasonable and are not unjustly or unreasonably discriminatory." *ARMIS Reporting Order*, 14 FCC Rcd. 11443, ¶ 32 (1999). Verizon has *not* shown either "good cause" for a waiver *or* that the detailed criteria for forbearance have been met.

First, as noted above, Verizon has *not* demonstrated that packet-switched services were ever intended to be within price caps, which is the *threshold* showing for pricing flexibility. *See* 47 C.F.R. § 69.701.

Second, section 69.729(a) of the Commission's pricing flexibility rules requires a LEC seeking pricing flexibility for a new service to "demonstat[e] . . . that the new service would be properly included in the price cap baskets and service bands for which the price cap LEC seeks pricing flexibility." Although Verizon lists its advanced packet-switched services as aligned with the High Capacity / DDS category in the Special Access Basket, *Verizon Mem.* at Att. B, it is not evident that the network capabilities associated with Frame Relay, ATM and other packet-switched services are the same as those traditional special access services in that category for which pricing flexibility has been granted. To the contrary, it appears, based on Verizon's assertions, that Frame Relay, ATM and other packet-switched services for which it seeks flexibility are *end-to-end* advanced services. *Verizon Mem.* at 11. It is not at all clear how the FCC's collocation test for pricing flexibility could even have applied to such integrated services. Thus, Verizon is incorrect in its belief that, but for its price cap waivers, it advanced packet services could have been included in the annual filing and entitled to a "me too" grant of pricing flexibility under section 69.729(a).

Tellingly, although Verizon quotes from paragraph 173 of the *Pricing Flexibility Order* (which tracks section 69.729(a)), Verizon fails to focus on section 69.729(b) of the rules that contains a categorical requirement that "[n]otwithstanding paragraph (a) of this section, a price cap LEC must demonstrate satisfaction of the triggers in § 69.711(b) to be granted pricing flexibility for any new

service that falls within the definition of a 'channel termination between a LEC end office and customer premises' as specified in § 69.703(a)(2)." Because Verizon is seeking flexibility for "packet switches *and* links that Verizon would use to provide its own Advanced Services," *Verizon Mem.* at 11 (emphasis added), it appears that end-user channel terminations are among the service components for which Verizon seeks relief. Thus, contrary to Verizon's assertion, it would *not* be entitled to a "me too" pricing flexibility grant, even if it could show that some of these services met the requirements of section 69.729(a).

Third, Verizon's waiver petition utterly fails to demonstrate any "special circumstances" warranting the requested relief. Although Verizon claims that it needs flexibility to compete with others' packet-switched services, Verizon has not identified a single instance in which the current regulatory structure has impeded its efforts to provide a packet-switched service. Verizon has not demonstrated that there is any real need – much less "special circumstances" – for the waiver requested for its Frame Rely, ATM and other packet-switched services (other than DSL). Although Verizon contends that "without pricing flexibility, Verizon is prevented from providing service and pricing offerings that are competitive with those of its competitors," *Verizon Mem.* at 14, it provides no evidence, exhibits, or supporting affidavits to suggest that any particular rule or regulation, absent a grant of flexibility, has posed any impediment to the reasonable rollout of any packet-switched service. Nor does Verizon allege that it has been unable to provide any specific service or respond to particular competitive circumstances. This is not surprising as Verizon, on November 20, 2003, touted its success in the advanced services enterprise market. "One year after Verizon announced an ambitious plan to

expand its high-speed data network nationwide, it has closed over 900 sales with more than 550 of its largest customers, including 65 Fortune 500 corporations as well as many educational institutions."[16] Verizon states that the "Securities Industry Association recently named Verizon its preferred vendor for domestic and international long-distance voice and data services, business continuity and disaster recovery, and Internet access services." *Id.* According to Eileen Eastman, vice president of the Yankee Group, whom Verizon quotes, "The customer response to Verizon's Enterprise Advance initiative indicates the market need for companies that can successfully offer communications diversity.... Customers need business continuity services, data storage, IP applications and transport, and Verizon has the infrastructure to deliver these. Verizon has already proven its capabilities in the local arena and is now taking that expertise across the country to support its customer base." *Id.* Notably, Verizon achieved these inroads *before* it announced that it began its "Aggressive Rollout of Advanced Services for Large Business, Government and Education Customers" beginning April 2004.[17]

Fourth, Verizon's general claims about competition for advanced services are *grossly insufficient* to justify a waiver or forbearance. Verizon does not give a breakdown as to the status of competition by service or scope. Most critically, Verizon fails to distinguish between local *and* interLATA advanced services in its cursory description of the status of competition. Verizon fails to offer any concrete evidence in

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[16] Enterprise Solutions News Release, November 20, 2003, *"Verizon Extends Winning Streak, Signing Over 900 Contracts for Enterprise Advance Services in First Year; Successful Initiative Spurs Ongoing Expansion of Nationwide Network as Company Becomes an 'All-Distance' Service Provider"* (available at www.verizon.com).

[17] Enterprise Solutions News Release, April 24, 2004, *"Verizon Plugs In New National Broadband Network; Aggressive Rollout of Advanced Services for Large Business,*

any actual relevant market, instead relying solely on an economically meaningless hodge podge of "national share" information. *See Verizon Mem.* at 8-9, 11-12. Verizon does not even attempt to argue seriously that there is meaningful "wholesale" competition for these advanced packet-switched services. Loops or channel terminations for Frame Relay, ATM and other packet-switched services are natural monopoly facilities that simply cannot be duplicated in most instances by competitive carriers, and the Bells have abused their market power to price special access well above their own economic cost of using those facilities.[18]

Verizon's contention that the advanced services market is "highly" or "especially competitive," and that IXCs rather than incumbent LECs hold the lion's share of the advanced services market, *Verizon Mem.* at 8, 10, 14, totally misses the point. As AT&T has previously demonstrated in numerous proceedings, Verizon and the other Bells enjoy market power in the provision of packet-switched broadband services.[19] Neither competitive carriers nor information service providers ("ISPs") have effective alternatives to the Bells for *wholesale* packet-switched broadband transmission facilities

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Government and Education Customers Begins This Month" (available at www.verizon.com).

[18] *Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services,* RM 10593, AT&T Corp. Petition, at 28-31 (Oct. 15, 2002) ("*AT&T Special Access Petition*"); *Triennial Review Order*, 18 FCC Rcd. 16798, ¶¶ 237-38, 302-05, 370-72 (2003).

[19] *See, e.g., Inquiry Regarding Carrier Current Systems, including Broadband over Power Line Systems*, ET Docket No. 03-104, Reply Comments of AT&T Corp. at 2-5 (Aug. 20, 2003) ("*AT&T BPL Reply Comments*"); *Ex Parte* Letter from David Lawson, counsel for AT&T Corp. to FCC, CC Docket Nos. 01-338, 96-98, 98-147, 96-149, dated Dec. 23, 2002, at 3-7 ("*AT&T Broadband Ex Parte*"); *AT&T Dom / Nondom Comments* at 19-50; *Review of Regulatory Requirements for Incumbent LEC Broadband Telecommunications Services*, CC Docket No. 01-337, Reply Comments of AT&T Corp. at 4-27 (Apr. 22, 2002) ("*AT&T Dom / Nondom Reply Comments*").

and services.[20] Verizon's and the other Bells' market dominance is pronounced in the small and medium business segment, where the incumbent LEC faces no significant competition in the provision of broadband services.[21] The Bells also continue to exercise market power over broadband services to large businesses through their bottleneck control of special access services.[22] Although AT&T and other competitive carriers would prefer to self-provide these last-mile facilities, the reality is that Verizon and the other incumbent LECs remain the only source for these facilities in the overwhelming majority of situations.[23] Indeed, AT&T "has a theoretically available, facilities-based alternative [to ILEC special access] in only about five percent of the buildings in which AT&T purchases special access."[24] The remainder is provided almost exclusively through the use of ILEC facilities.

Verizon suggests that it faces broadband competition from cable modem, fixed wireless and satellite service providers. *Verizon Mem.* at 12. Effective competition from cable does not exist. As AT&T recently explained in detail, Verizon faces, at best, *duopoly* competition in local geographic markets but that is patently insufficient to ensure

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[20] *AT&T BPL Reply Comments* at 2-3; *AT&T Broadband Ex Parte* at 4.

[21] *AT&T BPL Reply Comments* at 3.

[22] *AT&T BPL Reply Comments* at 4; *see also AT&T Corp., et al., Petition for a Writ of Mandamus*, No. 03-1397, at 17, 25-28, D.C. Circuit (filed November 5, 2003) ("*AT&T Mandamus Petition*"); *see generally AT&T Special Access Petition; Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM No. 10593, Reply Comments of AT&T Corp. (Jan. 23, 2003); *id.*, Ex. 2 (Decl. of Dr. Lee Selwyn) ("*AT&T Special Access Reply Comments*").

[23] *AT&T BPL Reply Comments* at 4.

[24] *AT&T Special Access Petition* at 28.

effective competition and constrain anticompetitive action by Verizon.[25] Even that limited competition arises from the provision of cable modem services as an alternative to DSL service; it does not reflect competition for the advanced services that are subject to Verizon's petition. Indeed, Verizon claims only that cable modem provides competition "for high-speed services in the large business market," *Verizon Mem.* at 12, but these services (and the putative illustrations of competition that follow) are not the ATM, Frame Relay, or VPN services subject to Verizon's petition, nor does cable modem-based services widely support such advanced, packet-based services.

The same flaws infect Verizon's reliance on "competition" from satellite and fixed wireless providers. *Verizon Mem.* at 12. Such services do not widely support or deliver packet-based services, and noticeably absent from Verizon's filing are any hard data on the shares enjoyed by these so-called "alternatives" in specific local markets. Moreover, even on a national scale, these alternative providers are not serious competitors even against DSL services. Combined, these platforms have only a

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[25] *IP-Enabled Services NPRM,* WC Docket No. 04-36, Reply Comments of AT&T at 35-45, filed July 14, 2004. *See* Remarks of Chairman Powell, Broadband Access Network Coordination Event (July 12, 2004) (additional broadband deployment required to "bring much-needed competition to DSL and cable"). Such duopoly competition is patently inadequate to prevent Verizon from acting on its incentives to ensure that rivals do not undercut its broadband offerings. "[W]here rivals are few, firms will be able to coordinate their behavior, either by overt collusion or implicit understanding." *FTC v. PPG Indus. Inc.*, 798 F.2d 1500, 1503 (D.C. 1986). *See also FTC v. University Health, Inc.*, 938 F.2d 1206, 1218 n.24 (11th Cir. 1991) ("Significant market concentration makes it easier for firms in the market to collude, expressly or tacitly."); *United States v. Ivaco, Inc.* 704 F. Supp. 1409, 1428 n.18 (W.D. Mich. 1989) ("with only two firms in the market, the firms would be able to police cheating, or non-collusive pricing by their competitor."). That is why "existing antitrust doctrine suggests that a merger to duopoly . . . faces *a strong presumption of illegality*." *EchoStar-DirecTV Merger Order*, 17 FCC Rcd. 20559, ¶ 103 (2002), (emphasis added); *id.* (separate statement of Chairman Powell) (duopolies "inevitably result in less innovation and fewer benefits to consumers" which "is the antithesis of what the public interest demands").

negligible and *declining* share of broadband services. *See, e.g., High Speed Services for Internet Access: Status as of December 31, 2003,* FCC Industry Analysis and Technology Division, Tables 1 - 4 (rel. June 2004). According to the Commission's statistics satellite/fixed wireless providers have seen their share of "high-speed" lines decline from 2.8% in 1999 to 1.3% in 2003, *id.*, Chart 6, and their share of "advanced service" lines decrease from 0.7% in 1999 to 0.3% to 2003, *id.*, Chart 8.[26]

In fact, the only two packet-switched services expressly addressed by Verizon are Frame Relay and ATM, two business services that are provided over Verizon's high capacity loops and transport facilities. Indeed, even Verizon admits that IXCs are dependent on ILEC special access to reach their own Frame Relay and ATM switches. *Verizon Mem.* at 11. Notwithstanding Verizon's claim (at 8) that advanced services competition is flourishing because long distance carriers control more than two-thirds of the *retail* market for Frame Relay and ATM, the competitive situation is no better for these services. In making this claim, Verizon inappropriately lumps together both local *and* interLATA data services. In the local markets where the Bells have been able to compete prior to grant of 271 relief, in contrast, they have already parlayed their control over bottleneck facilities into control of over 90% of the retail ATM and Frame Relay services provided to businesses – clear confirmation of enduring market power.[27] For example, information that Qwest has submitted to the FCC in another proceeding shows

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[26] Independent analyst estimates corroborate the Commission's numbers. Gartner, Inc., U.S. Consumer Broadband Keeps Growing: Online Households Remain Steady (Jan. 2, 2004), at 7 (In 2003, broadband modalities other than DSL and cable altogether accounted for only 4% to 6% of the market share.); In-Stat/MDR, Reaching Critical Mass: The US Broadband Market (Mar. 2004), at 19 (estimating satellite broadband subscribers to be 310,000 at the end of 2003).

[27] *AT&T BPL Reply Comments* at 3-5.

that the Bells account for 90.3% of Frame Relay local revenues, and 97% of ATM local revenues. The Bells' control over this essential input has enabled the Bells to dominate local data markets and, as they begin to capitalize on their new-found long distance authority, they will be able to leverage this market power outside their local monopolies as well.[28]

Fifth, because Verizon still exercises market power in the local advanced services market, granting Verizon pricing flexibility would increase its ability to "price squeeze" its competitors in the retail provision of advanced services and to engage in other anticompetitive conduct. As the Commission expressly found in the *Bell Atlantic / GTE Merger Order*, 15 FCC Rcd. 14,032, ¶ 5 (2000), "[t]he merger will increase the incentive and ability of the merged entity to discriminate against its rivals, particularly with respect to the provision of advanced telecommunications services...."[29] The basis for Verizon to achieve this result through an anticompetitive price squeeze is clear. Its ability to charge special access rates that are multiples of their forward-looking costs creates the textbook opportunity for a price squeeze against competitors dependent on special access services

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[28] As the Bells have shown with respect to long distance generally, their control of the local bottleneck permits them to grow share rapidly in the interLATA arena. For example, Verizon recently advised investors that, at the end of the first quarter of 2004, its long distance line penetration has reached 45 percent, with 32 percent year over year growth, and that its penetration of local/long distance packages has reached 51 percent, with 46 percent year over year growth. *See* Presentation of Tom Bartlett, Verizon, slide 16, Robert W. Baird & Co. 25th Annual Growth Stock Conference (May 4, 2004).

[29] *Bell Atlantic / GTE Merger Order*, ¶ 173 ("we conclude that incumbent LECs, such as Bell Atlantic and GTE, have the incentive and ability to discriminate against competitors in the provision of advanced services, interexchange services, and circuit-switched local exchange services, and that such incentive and ability will increase as a result of the merger. This increased incentive and ability to discriminate potentially creates a public interest harm because it may adversely affect national competitors' provision of services, and may force consumers to pay more for retail services, with reduced quality and choice.") (footnotes omitted); *see also id.* ¶ 183.

as an input. Access to last-mile transmission facilities is a "necessary input" for a broad array of local and long distance business services, including advanced, high speed packet-based services. Verizon can create an anticompetitive price squeeze by charging rivals a greater margin for access than the ILEC earns on its own integrated end-user services, and thereby deter efficient competitive supply of the retail service. Having attained pricing flexibility for its traditional special access services, which Verizon acknowledges its retail competitors use to offer their own packet-switched services, *Verizon Mem.* at 11, Verizon has raised the price for those services across the board. *See AT&T Special Access Reply Comments* at 4, 22-26 & Decl. of M. Joseph Stith. While Verizon can produce a price squeeze by increasing its retail competitors' input prices to levels that undermine retail competition in advanced services, its ability to achieve the price squeeze increases to the extent that Verizon can also selectively reduce its retail prices. And this price flexibility is, of course, precisely the ground on which Verizon justifies its petitions. *Verizon Mem.* at 7, 12. That is, Verizon is seeking to ensure that it can squeeze its retail competitors at both the wholesale level (by increasing input costs) and at the retail level (by selectively reducing retail prices for particularly important accounts).

The Commission has recognized the potential for both components of this type of price squeeze. As the Commission has explained, "[t]he incumbent ILEC could do this by raising the price of interstate access services to all interexchange carriers, which would cause the competing in-region carriers to either raise their retail rates to maintain their profit margins or to attempt to maintain their market share by not raising their prices to reflect the increase in access charges." *Access Reform Order*, 12 FCC Rcd. 15982, ¶ 277 (1997). Alternatively, "the incumbent LEC could also set its in-region,

interexchange prices at or below its access prices. Its competitors would then be faced with the choice of lowering their retail rates for interexchange services, thereby reducing their profit margins, or maintaining their retail rates at the higher price and risk losing market share." *Id.* And courts have also required the Commission to take care to ensure that carriers with market power cannot produce price squeezes because it is against the "public interest" for the Commission not to act to prevent price squeezes that "exert *any* anticompetitive effects, even if the monopolist's actions do not "absolutely preclude" competition.[30]

This anticompetitive threat is hardly fanciful, and Verizon utterly fails to address it in its petitions. By charging supracompetitive special access rates to IXCs, for example, the incumbents raise their rivals' costs in a disabling fashion. If IXCs try to pass these monopoly costs along to their customers, they risk losing customers to the Bells' long distance services that have last mile access available at economic costs. If they do not attempt to pass along the monopoly costs, they face artificially excessive costs that threaten to outrun revenues both in the short and long runs. *Access Reform Order*, ¶ 277. If IXCs and other providers of retail advanced services also must contend with selective price reductions as a result of the pricing flexibility Verizon now seeks, Verizon will be able to gain market share rapidly and reduce its competitors to levels below those required to compete effectively on a national level. Already, although the Bells have only recently entered long distance markets, they have gained business customers at an unprecedented rate. This parallels the Bells' behavior in consumer long distance markets. In just a few short years, the incumbents used their access

[30] *WorldCom Inc. v. FCC*, 308 F.3d 1, 10 (D.C. Cir. 2002).

advantage in consumer markets to go from zero market share to dominance of these markets – leading most recently to AT&T's announcement that it will no longer compete for mass market long distance customers. Prompt FCC action is necessary to prevent the incumbents from fully exploiting their access charge advantages in business markets and achieving the same anticompetitive results.

The fundamental reality is that Verizon's request for pricing flexibility, if granted, will *increase*, rather than minimize its incentive and ability to engage in anticompetitive pricing with respect to the packet-switched services. Indeed, the incentive to discriminate is heightened considerably where, as here, Verizon's packet-switched services in question employ local loop facilities, which in turn will give Verizon the ability to leverage its monopoly power over its fiber-based loops into related areas or services that utilize those same facilities.

Because of these indisputable facts, a grant of pricing flexibility, either through waiver or forbearance, would *neither* further *nor* be consistent with the public interest (a requirement for waiver and for forbearance under section 10(a)(3)), but rather would permit Verizon to engage discriminatory pricing (contrary to section 10(a)(1)), and a denial of its petitions is, in fact, necessary to protect consumers so as not to choke off competition for advanced services and thereby limit consumer choice and ultimately expose consumers to noncompetitive pricing (section 10(a)(2)). As noted earlier, it is *Verizon's* burden in this proceeding to present empirical evidence enabling the "painstaking analysis of market conditions" that § 10(a) demands. *WorldCom*, 238 F.3d at 459; *AT&T*, 236 F.3d at 735-37. Absent such market-specific evidence, the

Commission cannot determine the extent of Verizon's monopolies – and, therefore, cannot make the findings necessary to justify forbearance, or waiver.

Moreover, the Commission should realize that through its price cap waivers, Verizon has *already* achieved substantial flexibility for its advanced services by keeping them outside of its price cap baskets – pricing relief that a carrier would typically only get once it has achieved Phase II pricing flexibility.[31] What Verizon wants now is the ability to offer contract tariffs to select customers. Not being subject to price caps, Verizon was not able to bootstrap, however illicitly, new advanced services into its earlier grants of pricing flexibility through the annual filing mechanism. Now, however, Verizon discovers that it wants to engage in "customized pricing and discounts and flexible contract terms," *Verizon Mem.* at 12, all of which it wants without having to make any sort of detailed competitive showing at all. There is no good cause or public interest benefit for this result. To the contrary, such relief would permit Verizon to wield its market power, create price squeezes for advanced services offered by others, and would make such anticompetitive behavior harder to detect.

III. THE COMMISSION SHOULD NOT EXPAND PRICING FLEXIBILITY TO ADVANCED SERVICES AT THIS TIME.

Although Verizon has already gotten substantial relief from price regulation for its packet-switched services in the guise of its interim waivers, this is not the time to grant further relief that would allow it to exercise pricing flexibility through offering contract tariffs.

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[31] In addition, Verizon has also obtained waivers from sections 61.38 and 61.49. *See Verizon Petition for Waiver of Sections 61.42(g), 61.38 and 61.49 of the Commission's Rules,* 17 FCC Rcd. 11010, ¶ 3 (2002) (citation omitted).

First, the Commission is considering further relief for incumbent LECs' broadband services in the *Dom / Nondom* and *Wireline Broadband* proceedings. Underpinning Verizon's request for relief is its assumption that it *is* nondominant in the provision of advanced services. That issue, however, has not been decided and is squarely before the Commission in the *Dom / Nondom NPRM*. That proceeding contains thousands of pages of record evidence regarding the question of whether incumbent LECs have market power in any of the to-be-determined markets, and on the appropriate regulatory requirements that should govern the provision of broadband services. Indeed, the evidence is overwhelming that Bell companies continue to have market power in local markets, including the provision of special access services.

Second, as AT&T and others have repeatedly demonstrated both before the FCC and the courts, the test that the Commission adopted in the *Pricing Flexibility Order* does *not* test for the presence of price-constraining competition, and a grant of pricing flexibility would allow Verizon to raise or drop rates for its packet-based services without any pricing constraints. This is inappropriate because the Bells have used their control over special access to reap monopoly rents, put competitors in a price squeeze, and foreclose competitive broadband offerings.[32] Where the Commission has mistakenly granted the Bells special access pricing relief, they have responded by charging rates that are generally above those that are still under price caps, which by itself refutes any claim that a competitive market exists for last-mile access services, such as the loop-based

[32] *AT&T Special Access Reply Comments* at 43-47 & Decl. of Janucz A. Ordover and Robert D. Willig, at ¶¶ 66-74; *see also AT&T Dom / Nondom Comments* & Decl. of Alan Benway, at ¶¶ 11, 13, 15-17 (In 17 out of 28 markets evaluated, the ILEC special access rate exceeded AT&T's retail rate for local Frame Relay service, and in almost two-thirds of the markets surveyed, AT&T's local ATM service rate.).

packet-switched services contemplated in this proceeding. Indeed, a study filed with the Commission on June 12, 2003, concludes that the Bells are reaping at least $5.6 billion in windfall profits annually through this last-mile monopoly.[33] Given this fact, and given the pendency of the Special Access Mandamus before the Court of Appeals – a proceeding in which AT&T and numerous other parties have demonstrated the critical need for the Commission to reexamine the disastrous consequences of the *Pricing Flexibility Order* and premature deregulation of special access services – the Commission should be developing a more stringent test and require Verizon to comply with that before allowing any additional flexibility.

Even assuming the pricing flexibility regime applied to advanced services offering through an incumbent LEC's operating company (which it does *not*) and if the Commission were even inclined to consider a grant of pricing flexibility for Verizon's advanced packet-switched services (which it should *not*), it is fundamental that, at a minimum, Verizon must be required to show, using a detailed analysis of local market conditions, that such pricing flexibility is justified. This is particularly critical given the radical change in market conditions since the FCC adopted the 1999 *Pricing Flexibility Order*. The FCC had issued its *Pricing Flexibility Order* at the height of the boom in telecommunications that occurred in response to the Telecommunications Act of 1996 and the explosion of dot.coms in the late 1990s. During this era, start-up companies like Qwest, Global Crossing, Xo and others had announced plans to construct alternative networks and had raised hundreds of millions of dollars in capital. Almost immediately

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[33] *See* Rappoport, Taylor, Menko, Brand, *Macroeconomic Benefits from a Reduction in Special Access Price* (Jun. 12, 2003), filed in RM Docket No. 10593, at 5. *See also AT&T Mandamus Petition* at 17, 25-28; *AT&T BPL Reply Comments* at 4 n.12.

thereafter, the bubble burst; access to capital evaporated; and scores of firms that had announced ambitious plans to construct alternative transmission networks ceased operations or went into bankruptcy. *See, e.g.*, *AT&T Special Access Reply Comments* at 18-20. Thus, it is critical that Verizon be required to demonstrate local competition sufficient to justify pricing flexibility today, given that competitive conditions are likely to have changed since Verizon's earlier grants of pricing flexibility.[34] Whatever administrative burdens this process may impose on Verizon pales in comparison to the further harm to competition that would occur if the Commission were to grant Verizon pricing flexibility without making any such showing at all.

In light of the foregoing, AT&T respectfully suggests that the most prudent course is to *reject* Verizon's unsupported waiver and forbearance requests and comprehensively address the appropriate regulation of packet-switched services through the *Dom / Nondom NPRM* and related proceedings.

[34] *See, e.g., Verizon Petitions for Pricing Flexibility for Special Access and Dedicated Transport Services*, 16 FCC Rcd. 5876 (2001).

CONCLUSION

Thus, for the reasons stated above, both Verizon's petition for waiver and its petition for forbearance should be *denied.*

Respectfully submitted,

/s/ Judy Sello
Leonard J. Cali
Lawrence J. Lafaro
Judy Sello
AT&T Corp.
Room 3A229
One AT&T Way
Bedminster, NJ 07921
(908) 532-1846

Its Attorneys

August 3, 2004

CERTIFICATE OF SERVICE

I, Tracy E. Rudnicki, hereby certify that on this 3rd day of August 2004, the foregoing AT&T Opposition To Verizon's Petitions For Waiver Or, Alternatively, Forbearance To Allow It To Exercise Pricing Flexibility For Fast Packet Services was served on the following parties.

/s/ Tracy E. Rudnicki

Marlene H. Dortch
Office of the Secretary
Federal Communications Commission
445 12th Street, S.W.
Suite TW-A325
Washington, DC 20554
(Via ECFS)

Marvin F. Sacks
Pricing Policy Division
Wireline Competition Bureau
Federal Communications Commission
445 12th Street, S.W.
Room 5-A221
Washington, DC 20554
(Via E-mail)

Best Copy and Printing
Portals II
445 12th Street, S.W.
Room CY-B402
Washington, D.C. 20554
(Via E-mail)

Deena Shetler, Deputy Division Chief
Pricing Policy Division
Wireline Competition Bureau
Federal Communications Commission
445 12th Street, S.W.
Room 5-A221
Washington, DC 20554
(Via E-mail)

Michael E. Glover
Edward Shakin
Joseph DiBella
Verizon
11515 N. Court House Road, Suite 500
Arlington, VA 22201-2909
(Via U.S. Mail)

Gregory J. Vogt
Joseph M. Ward
Wiley Rein & Fielding, LLP
1776 K Street, NW
Washington, D.C. 20006
(Via Hand Delivery)